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FM AMEMBASSY COLOMBO  
TO SECSTATE WASHDC 4483  
INFO DEPT OF TREASURY WASHDC  
USDOC WASHDC  
AMEMBASSY NEW DELHI  
AMCONSUL CHENNAI  
AMCONSUL MUMBAI  
AMEMBASSY ISLAMABAD  
AMEMBASSY DHAKA  
AMEMBASSY OSLO  
AMEMBASSY LONDON  
AMEMBASSY TOKYO  
AMEMBASSY MANILA  
USCINCPAC HONOLULU HI  
DIA WASHDC  
NSC WASHDC

UNCLAS SECTION 01 OF 03 COLOMBO 000172

MANILA FOR USADB

E.O. 12958: N/A

TAGS: [ECON](#) [PREL](#) [PTER](#) [PGOV](#) [CE](#)  
SUBJECT: SRI LANKA: THE LTTE BUILDS A FINANCIAL INFRASTRUCTURE

REF: 02 COLOMBO 996 (NOTAL)

**¶1. SUMMARY:** DUE TO AN INTERNATIONAL CRACKDOWN ON TERRORIST FINANCING POST SEPTEMBER 11, THE LIBERATION TIGERS OF TAMIL EALAM (LTTE) HAS SHIFTED OVER THE PAST YEAR FROM FOREIGN FUND-RAISING TO LARGELY DOMESTIC FINANCING. WHILE THE LTTE TRADITIONALLY LEVIED TAXES IN AREAS UNDER ITS CONTROL, RECENTLY IT HAS DEVISED NEW AND MORE SOPHISTICATED MEANS OF RAISING REVENUE. ACCORDING TO RECENT MEDIA REPORTS, THE FINANCE DIVISION OF THE LTTE IS ONE OF THE MOST POWERFUL ARMS OF THE REBEL GROUP. THE TWO KEY INSTITUTIONS OF THE LTTE FINANCE ARM ARE "EELAM CUSTOMS" AND THE "TAMIL EELAM BANK," BOTH OF WHICH OPERATE IN LTTE HELD AREAS IN THE NORTH. THE LTTE'S DEVELOPMENT OF A DISTINCT FINANCIAL SYSTEM WITHIN THE BORDERS OF SRI LANKA OFFERS AN INDICATION OF THE DEGREE OF AUTONOMY THE ORGANIZATION WOULD LIKELY EXPECT IN ANY FEDERAL SOLUTION TO THE ISLAND'S ETHNIC CONFLICT. END SUMMARY.

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FUND-RAISING SHIFTS INWARD  
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**¶2.** IN THE YEARS SINCE LARGE-SCALE ETHNIC CONFLICT BROKE OUT IN 1983, THE LTTE HAS FINANCED ITSELF MOSTLY THROUGH FUND-RAISING ABROAD. SYMPATHETIC MEMBERS OF THE TAMIL DIASPORA - PARTICULARLY IN CANADA, THE UK AND AUSTRALIA - DONATED TO THE CAUSE OF A SEPARATE TAMIL HOMELAND. SINCE SEPTEMBER 11, 2001 THE LTTE HAS FOUND IT INCREASINGLY DIFFICULT TO RAISE MONEY ABROAD. AS A DESIGNATED FOREIGN TERRORIST ORGANIZATION (FTO), THE LTTE HAS SEEN ITS FUNDING DRY UP SUBSTANTIALLY AMIDST THE US-LED INTERNATIONAL CRACKDOWN ON TERRORIST FINANCE.

**¶3.** AS FOREIGN FUNDS HAVE EVAPORATED, THE LTTE HAS LOOKED FOR WAYS TO RAISE MONEY AT HOME. WHILE THE LTTE HAS LONG LEVIED TAXES IN AREAS UNDER ITS CONTROL, IT IS NOW BUILDING A SOPHISTICATED FINANCIAL INFRASTRUCTURE THAT ALLOWS IT TO COLLECT REVENUE AND REGULATE COMMERCE ON A LARGE SCALE. WHILE THE LEVEL OF TAXATION IS AN ADDED BURDEN ON THE LONG-SUFFERING RESIDENTS OF SRI LANKA'S NORTH AND EAST (SEE REFTEL), THE LTTE DEFENDS ITS ACTIVITIES SAYING FUNDS ARE NEEDED TO MAINTAIN THE ORGANIZATION AND ITS CADRES, INCLUDING THE WAR WOUNDED.

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EELAM CUSTOMS: THE LTTE'S CASH COW  
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**¶4.** ACCORDING TO REPORTS AND SOURCES IN JAFFNA, THE LTTE'S TAX ARM IS REACHING INTO ALMOST EVERY FACET OF LIFE IN THE

NORTH, WITH THE MAIN SOURCE OF FUNDS COMING FROM THE LTTE CUSTOMS DEPARTMENT. THE LTTE CUSTOMS OFFICE IS LOCATED IN OMANTHAI ALONG THE A-9 ROAD, WHICH LINKS JAFFNA TO THE SOUTH. ALL COMMERCIAL SHIPMENTS ENTERING THE NORTHERN PROVINCE ARE UNLOADED, CHECKED AND TAXED AT THIS POINT. THE LTTE OPERATES A MULTI-BAND TAX STRUCTURE BETWEEN 5% AND 25%. FOOD ITEMS ARE GENERALLY TAXED AT 7%, CONSUMER ITEMS AT 10%, CONSTRUCTION MATERIAL AT 15% AND NON-ESSENTIALS BETWEEN 20-25%. THERE IS A TAX OF 10% ON MOTOR VEHICLES TAKEN TO THE NORTHERN PROVINCE FOR PERMANENT USE. MEDICINE IS DUTY FREE. THE TAX SYSTEM WAS PUBLICLY ANNOUNCED IN JUNE 2002 IN "SUDAROLI," A PRO-LTTE, TAMIL LANGUAGE DAILY.

15. IN ADDITION TO THE TAX ON GOODS, TRUCKS ARE CHARGED RS 2,500 (APPROX \$25) PER TRIP. EVEN GOVERNMENT DEPARTMENTS, SUCH AS THE COOPERATIVE WHOLESALE ESTABLISHMENT (CWE) WHICH OPERATES A RETAIL STORE IN JAFFNA, PAY THE LTTE TAXES WHEN TRANSPORTING GOODS BY ROAD. GOODS TRANSPORTED FOR OFFICIAL USE SUCH AS TO GOVERNMENT BANKS, UNIVERSITIES AND DONOR-FUNDED PROJECTS ARE EXEMPTED. ARTICLES MEANT FOR PERSONAL USE ARE NOT TAXED EXCEPT FOR SOME ELECTRICAL ITEMS AND LIQUOR. FURTHER, TRAVELERS TO THE NORTHERN PENINSULA ARE TAXED RS 350 (\$3.50) PER PERSON. EXPATRIATE TAMILS TRAVELING TO JAFFNA THROUGH OMANTHAI ARE SUPPOSEDLY CHARGED RS 500 (\$5) PER FAMILY. GSL EMPLOYEES TRAVELING FOR OFFICIAL WORK ARE SPARED THE TAX.

16. IN ADDITION TO THESE CUSTOMS LEVIES AT OMANTHAI, THE LTTE IS TAXING COMMERCE IN SEVERAL OTHER WAYS. FOR INSTANCE, TRADERS HAVE TO PAY THE LTTE A FIXED FEE, USUALLY EVERY SIX MONTHS. GSL EMPLOYEES IN THE EASTERN PROVINCE PAY A 7% INCOME TAX. A SOURCE AT A CONSTRUCTION FIRM OPERATING IN JAFFNA CONFIRMED THAT THE COMPANY PAYS A TAX OF 5% OF CONTRACT VALUE TO THE LTTE. GUESTHOUSES AND INDIVIDUALS RENTING OUT ROOMS ARE ALSO TAXED. FURTHERMORE, THE LTTE OCCASIONALLY CONDUCTS SPECIAL CAMPAIGNS AND RALLIES TO COLLECT MONEY FROM TRADERS, BUSINESSMEN AND WORKERS. WHEN THE LTTE TAX COLLECTOR KNOCKS ON YOUR DOOR FOR A "SPECIAL CAMPAIGN," THE SENSIBLE CITIZEN READILY PAYS UP.

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BANK OF TAMIL EELAM: SRI LANKA'S OTHER STATE BANK  
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17. THE LTTE ALSO OPERATES A BANKING NETWORK UNDER THE NAME BANK OF TAMIL EELAM (BOTE). ACCORDING TO PRESS REPORTS AND SOURCES IN JAFFNA, THE BANK HAS FIVE BRANCHES IN LTTE CONTROLLED AREAS, ALTHOUGH IT HAS NO LICENSE FROM THE CENTRAL BANK OF SRI LANKA, WHICH IS THE SOLE MONETARY AUTHORITY IN SRI LANKA. BOTE WAS FIRST ESTABLISHED ABOUT 10 YEARS AGO WHEN THE GSL IMPOSED ECONOMIC SANCTIONS ON LTTE CONTROLLED AREAS. IN THE LTTE ADMINISTRATIVE CAPITAL KILINOCHCHI, THE BOTE IS SITUATED JUST OPPOSITE THE BRANCHES OF TWO GSL STATE OWNED BANKS, BANK OF CEYLON AND PEOPLE'S BANK. THE BOTE BRANCH IN KILINOCHCHI HAS OVER 10,000 ACCOUNT HOLDERS, MOSTLY RETURNING REFUGEES. ACCORDING TO MEDIA REPORTS, THE LTTE ENCOURAGES PEOPLE TO BANK WITH THE BOTE, AND MUCH OF THE BOTE BALANCE SHEET CONSISTS OF LTTE DEPOSITS (PROCEEDS FROM TAX COLLECTION). BOTE'S SUCCESS IN ATTRACTING DEPOSITS IS ALSO ATTRIBUTED TO HIGHER INTEREST RATES, A VARIETY OF CREDIT FACILITIES AND CONVENIENCE. FOR INSTANCE, THE BANK IS OPEN EVEN ON PUBLIC HOLIDAYS WHEN OTHER BANKS ARE CLOSED. IN SPITE OF FUNCTIONING WITHOUT GOVERNMENT APPROVAL, THE BANK OFFERS MANY CONVENTIONAL BANKING FACILITIES SUCH AS FIXED DEPOSITS, CURRENT ACCOUNTS, SAVING ACCOUNTS AND FOREIGN EXCHANGE SERVICES. IT ALSO OFFERS PAWNING FACILITIES, AND LOANS FOR HOUSING AND BUSINESS. AS IN ANY OTHER BANK, IT ISSUES CHEQUE BOOKS AND MONTHLY STATEMENTS TO CUSTOMERS.

18. PRESIDENT CHANDRIKA KUMRANATUNGA RAISED THE ISSUE OF LTTE TAXES IN SEPTEMBER 2002 AFTER THE JAFFNA MUNICIPAL COUNCIL AND SEVERAL OTHER LOCAL BODIES IN THE NORTH PASSED RESOLUTIONS CONDEMNING THE ILLEGAL TAXES. A GROUP OF PARLIAMENTARIANS HAVE ALSO RAISED THE ISSUE OF THE ILLEGAL OPERATION OF THE BOTE. THE GSL HAS NOT SO FAR INTERFERED WITH THE ILLEGAL BANKING OPERATIONS, CLAIMING IT DOES NOT

HAVE CONCLUSIVE PROOF OF THEIR EXISTENCE. THE DIRECTOR OF BANK SUPERVISION OF THE CENTRAL BANK OF SRI LANKA TOLD THE EMBASSY THAT THE CENTRAL BANK HAS NOT INVESTIGATED OPERATIONS OF THE BOTE IN LTTE CONTROLLED AREAS. POLICE SOURCES HAVE SAID THAT BOTE IS NOT FUNCTIONING IN AREAS UNDER GSL CONTROL.

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COMMENT  
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¶ 9. THE LTTE APPEARS TO BE METHODICALLY DEVELOPING A PARALLEL FINANCIAL SYSTEM WITHIN SRI LANKA'S BORDERS. UNFORTUNATELY, THE LTTE IS BUILDING A HEAVILY REGULATED, HEAVILY TAXED AND LARGEY CLOSED ECONOMY. THE OFFICIAL SRI LANKAN ECONOMY, BY CONTRAST, IS TRADE-BASED AND BY FAR THE MOST OPEN IN SOUTH ASIA. THESE DIVERGENT FINANCIAL SYSTEMS THREATEN TO INCREASE THE ALREADY ALARMING DISPARITY IN STANDARDS OF LIVING IN COLOMBO VS. THE NORTH/EAST - A WORRYING PROSPECT FOR THE FUTURE OF THE PEACE PROCESS.

¶ 10. MOREOVER, THE LTTE SHOWS NO SIGNS OF BEING WILLING TO DISMANTLE THE FINANCIAL INFRASTRUCTURE IT IS DEVELOPING. THE LTTE'S HOMEGROWN ECONOMIC POLICY - COMPLETE WITH CUSTOMS DUTIES TO ENTER "EELAM" TO A "STATE"-RUN BANK - SHOWS THE DEGREE OF REGIONAL AUTONOMY IT LIKELY ENVISAGES AS PART OF ANY FEDERAL SOLUTION TO THE ETHNIC CONFLICT. IT IS A VISION OF REGIONAL AUTONOMY THAT MAY BE FAR DIFFERENT FROM THAT OF GSL - A YAWNING GAP THAT ILLUSTRATES THE CHALLENGES AHEAD IN THE PEACE PROCESS.

WILLS